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Policy Brief.....Background on Refundability of the Child Tax Credit

Congressional Democrats have recently seized on a report from the Center on Budget and Policy Priorities (see end of this document for information about this group) to argue for passage of a Senate provision to accelerate an increase in the refundability of the child tax credit. This document seeks to provide some background on this issue.

Current Law Regarding Refundability of the Child Tax Credit:

According to the Joint Committee on Taxation: "For 2003, the child credit is refundable to the extent of 10 percent of the taxpayer's earned income in excess of \$10,500 (indexed for inflation). The percentage is increased to 15 percent for taxable years 2005 and thereafter. Families with three or more children are allowed a refundable credit for the amount by which the taxpayer's social security taxes exceed the taxpayer's earned income credit, if that amount is greater than the refundable credit based on the taxpayer's earned income in excess of \$10,500 (for 2003). The refundable portion of the child credit does not constitute income and is not treated as resources for purposes of determining eligibility or the amount or nature of benefits or assistance under any Federal program or any State or local program financed with Federal funds."

It is important to remember that when a tax credit is refundable, it means that the taxpayer, even if they owe no taxes, can receive a "refund" check from the government. In other words the government is giving money out to people who do not pay taxes.

Current law could be appropriately described as an income related cap on the amount of a "refund" a taxpayer can receive as a result of the refundable portions of the child tax credit.

It should be noted that we also phase-out the child tax credit for taxpayers as their income increases. Again, according to the Joint Committee on Taxation: "The child tax credit is phased out for individuals with income over certain thresholds. Specifically, the otherwise allowable child tax credit is reduced by \$50 for each \$1,000 (or fraction thereof) of modified adjusted gross income over \$75,000 for single individuals or heads of households, \$110,000 for married individuals filing joint returns, and \$55,000 for married individuals filing separate returns. The length of the phase-out range depends on the number of qualifying children. For example, the phase-out range for a single individual with one qualifying child is between \$75,000 and \$85,000 of modified adjusted gross income. The phase-out range for a single individual with two

qualifying children is between \$75,000 and \$95,000. The amount of the tax credit and the phase-out ranges are not adjusted annually for inflation.”

Senate Proposal:

Accelerate the increase from 10 percent to 15 percent for 2003 and 2004.

Conference Report Enacted Into Law:

Drops the Senate provision thus maintaining current law.

Is it true that no low-income families will receive an increase in the refundable portion of the child tax credit? That is not true; some, but not all families will see an increase in the amount of the refundable child tax credit they receive. Even the liberal Center on Budget and Policy Priorities (which released the study being used by Democrats) admits that some families will receive an increase in the refundable portion of their child tax credit:

Similarly, some increases in refundable *child credit* outlays occur under the new law, for two reasons. First, in the same way that EITC outlays will rise due to the enactment of other tax-cut provisions, the reductions in income tax liability that result from other tax cuts also will lower the portion of the child tax credit needed to offset some families' income tax liability, and will thereby increase the amount of child tax credit benefits provided as refunds. Second, some low-to-moderate income families with incomes modestly above the income ranges shown in the table on page 2 *are* affected by the current \$600-per-child ceiling on the child tax credit and will see an increase in their refundable child credit as a result of the increase in the child credit to \$1,000 per child.

Consider, for example, a married couple with one child and income of \$18,000 in 2003. Prior to enactment of the new legislation, this couple would have owed \$90 in taxes in 2003 before its child tax credit was figured. The family would have received a child tax credit of \$600, with \$90 of it going to eliminate the family's tax liability and the remaining \$510 provided in refundable form. Under the new law, this family's pre-child credit tax liability is reduced to zero because of the increase in the standard deduction for married couples. **The family now qualifies for a refundable child tax credit of \$750 (10 percent of the amount by which its \$18,000 income exceeds the \$10,500 refundability threshold), and all \$750 will be provided in refundable form. The family's total child credit will rise from \$600 to \$750, while the amount of its credit that is provided in refundable form will rise by a somewhat larger amount, from \$510 to \$750.**

<http://www.cbpp.org/5-28-03tax3.htm>

In other words, whether or not a family will receive an increase in their child-tax credit refund depends upon the underlying tax situation of the family.

Impact of adopting the Senate proposal to accelerate the increase in refundability?

Adoption of the Senate proposal would increase government outlays (spending) by approximately \$3.5 billion. If this proposal was “offset” by increasing taxes on businesses as some Senate Democrats have proposed, we would be raising taxes on some to increase spending for others, or in other words redistributing wealth.

Information about the Center on Budget and Policy Priorities:

Members of the CBPP Board of Directors include individuals from the Brookings Institution, Children's Defense Fund, and the Urban Institute – all of which are considered liberal organizations.

How accurate is the CBPP?

THE NEW WELFARE LAW

by David A. Super, Sharon Parrott, Susan Steinmetz, and Cindy Mann

Center on Budget and Policy Priorities

August 13, 1996

“The overriding effect of the legislation is likely to be a large increase in poverty, especially among children and legal immigrants.”

In reality, 1.7 million children were living in poverty in 2001, compared to 14.7 million in 1995, according to the Census Bureau. Census Bureau data also shows that 30.9% of foreign-born non citizens were in poverty in 2001, compared to 34.9% in 1997.

Quotes about the CBPP:

The Los Angeles Times referred to the CBPP as “liberal-leaning” on May 30 (<http://www.latimes.com/news/nationworld/nation/la-na-taxes30may30,1,117598.story>) and as one of several “liberal interest groups” critical of the tax bill’s treatment of low-income children on June 3 (<http://www.latimes.com/news/nationworld/nation/la-na-taxes3jun03,1,1860657.story>).

The New York Times has referred to the CBPP as “a liberal group” and “a liberal research group” (May 29 and June 1).

ABC News refers to the CBPP as “a liberal policy group” (http://more.abcnews.go.com/sections/wnt/Business/taxbill030529_childcredit.html), while CBS News calls the Center “a very liberal think tank” (<http://www.cbsnews.com/stories/2001/06/01/politics/main294323.shtml>).
